

DOCKET SECTION

NFN-T-1

BEFORE THE
POSTAL RATE COMMISSION
WASHINGTON, D.C. 20268-0001

DEC 30 3 26 PM '97

POSTAL RATE AND FEE CHANGES, 1997

Docket No. R97-1

TESTIMONY OF

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CONCERNING RATES FOR NONPROFIT STANDARD MAIL (A)

ON BEHALF OF

NATIONAL FEDERATION OF NONPROFITS

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December 30, 1997

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Autobiographical Sketch

My name is Carolyn A. Emigh. I am a principal in the Non-profit Service Group ("NSG"), a consulting firm that provides legal, economic, accounting, and management consulting services to nonprofit organizations. NSG has its headquarters at 1250 24th Street, NW, Suite 400, in Washington, DC 20037.

I was graduated from Pitzer College, a member of the Claremont Colleges, in Claremont, CA, in 1970 with a concentration in economics and international relations. In 1969, I studied at the Institut d'Etudes Francaises in Avignon, France. In 1972, I completed the two-year graduate program at The John Hopkins University School of Advanced International Studies in Washington, DC and Bologna, Italy.

I have also studied industrial organization (antitrust economics) at the graduate level at The George Washington University and currently am a third year student at the School of Law at Washington University in St. Louis, MO. The late Dr. W. Edwards Deming was my mentor in the application of statistical methods to management of business, industry, and government.

From 1972 to 1980, I served in the United States Senate and House of Representatives. In the Senate, I was Economic Policy Advisor to the Majority Leader. I served as professional staff economist to the Oversight and Investigations Subcommittee of the House Interstate and Foreign Commerce Committee.

Since 1981, I have assisted the National Federation of Non-profits (formerly the Nonprofit Mailers Federation) to represent the interests of nonprofit mailers before the United States Congress, federal agencies, state government, and self-regulatory organizations.

I have testified before the Postal Rate Commission in Docket Nos. R84-1, R90-1, R94-1 and in various regional hearings that the Commission conducted in 1986 as part of its study of preferred mail rates.

I. Overview

A. Fair and equitable nonprofit rates: Congressional policy reflects historical results.

A regulated rate scheme should be perceived to produce fair rates. Two pieces of mail--each having the same handling characteristics, and each receiving the same level of service--should pay the same rate, all other things being equal.

In the case of commercial and nonprofit Standard A mail, ratepayers expect to pay different rates for two reasons. First, historically nonprofit mailers tend to produce consistently lighter weight, more uniformly shaped pieces of mail than do their commercial counterparts. Thus, the "attributable" (or "direct") cost to process the nonprofit Standard A mail stream was--and still is--substantially less than the direct costs to handle the commercial Standard A mail stream.

Second, in the Revenue Forgone Reform Act, Congress directed rate regulators to set the "institutional" (or "overhead") costs of nonprofit mail at no more than one-half of the mark up used to assign the Postal Service's overhead costs to the comparable rate category of commercial mail. The policy objective was that nonprofit mail should be charged less than the comparable commercial rate within each rate category, but nonprofit rates should move in tandem with their respective comparable commercial rate.

Thus, everyone expects that mail that serves a nonprofit purpose will pay a lower rate than the comparable commercial

piece. That's because the direct cost to handle the nonprofit Standard A mail stream is lower, and the mark up for overhead costs may be no more than one-half of the mark up of commercial Standard A rates.

With respect to adjustments in nonprofit rates as a result of periodic rate cases, nonprofit rates tended to move roughly in tandem with the comparable commercial rate. Mailers came to expect this kind of symmetry in the differential between a nonprofit rate and its comparable commercial counterpart. Historically, the nonprofit rate has been about one-half of the comparable commercial rate. This experience was captured in part in the Revenue Forgone Reform Act and executed by it.

Although the respective rate escalators might not have been identical for both the nonprofit and comparable commercial rate, they were close enough over the years to evoke a sense of fairness. At least it seemed that the Postal Service and the Postal Rate Commission treated the two groups of Standard A mail evenhandedly.

B. Evidence of discriminatory pricing

An analysis of the rate of increase or decrease that the Postal Service proposes for each of the 26 rate categories of Standard A mail reveals that, in almost 90 percent of the categories, the proposed rates of change for nonprofit and comparable commercial rates are asymmetrical.

Postal management's proposal departs from both the historical

relationship between nonprofit and commercial Standard A rates and from the relationship that Congress envisioned when it enacted the Revenue Forgone Reform Act. That the Postal Service has departed from this historical sense of fairness is unfortunate for a number of reasons.

One reason is that, uncorrected, nonprofit organizations will be compelled to find a way to inject fairness back into the rate scheme. One way is for Congress to make the policy subsumed in the Revenue Forgone Reform Act more explicit.

The Postal Service proposal departs from the historical relationship in that it seeks to adjust some of the rates of otherwise comparable nonprofit and commercial pieces in opposite directions. That is, postal management proposes to increase the rate for a piece of nonprofit mail and roll back the rate for a comparable piece of commercial mail. In these instances, the differential that postal management proposes between the two disparate rates of change is enormous. Table I below quantifies these proposed differentials.

In other instances, postal management proposes to raise or lower the rate for both nonprofit and commercial pieces within the same rate category, but the proposed differential is so large as to be discriminatory on its face. Part II of this document quantifies the rates of change between comparable nonprofit and commercial pieces of mail.

Because handling, hence costing, characteristics are virtu-

ally identical for nonprofit and commercial mail within a particular rate category, the proposed asymmetrical pricing treatment strongly suggests that the resulting rate schedule discriminates against nonprofit Standard A mail in favor of comparable commercial pieces.

- (1) For Standard A mail that costs the most to process, postal management proposes that nonprofit mail underwrite a rate rollback for commercial mail.

Consider the proposed rate of change for the non-automated, basic rate category for letter size mail. That's mail that fails to qualify for processing by the automated sorting equipment and that the mailer--nonprofit or commercial--presorts only to the minimum extent required to qualify for Standard A rates.

Whether the piece of mail serves a nonprofit or commercial purpose, postal workers will have to do a comparable amount of work in order to process each piece of mail in that rate category, yet postal management proposes to raise the rate for the nonprofit piece by 20 percent and roll back the rate for the commercial piece by 4 percent. That's a whopping 24 percentage point differential for mail that essentially has the same handling characteristics. It's classic price gouging.

- (2) Automation rate categories: Postal management's proposed rates blatantly discriminate against nonprofit mail.

What is particularly disconcerting is postal management's

disparate treatment within the Standard A rate categories of mail that qualify for processing by the automated sorting equipment. Postal management repeatedly promised rate reductions, or at least to slow down the rate of increase, for mailers who financed the tremendous costs to produce mail that the automated sorting equipment could read and process at optimum speed.

With one exception, postal management's proposal makes good on that promise for commercial Standard A mail, but they would penalize the comparable nonprofit piece. Again, this is discriminatory on its face. The automated processing equipment cannot distinguish between a piece of a mail that serves a nonprofit as opposed to a commercial purpose.

The one exception is the automation rate category within the Enhanced Carrier Route Subclass for letters. There, postal management seeks to raise the rate for both nonprofit and commercial by eight percent, an amount that's between three and four times as great as the rate of increase of inflation. The magnitude of that proposed increase, coming on top of the cost to prebarcode and sort by carrier route, sounds like a penalty, not a reward, in that case for both nonprofit and commercial Standard A mail.

In contrast, both commercial and nonprofit Standard A mailers, but particularly nonprofits, kept their end of the bargain. Since reclassification, about 45 percent of nonprofit Standard A mail pays the "Automation Presort" rate versus 37 percent of commercial Standard A mail, according to the Postal Service's compilation called "Revenue, Pieces, and Weight by

Classes of Mail" for fiscal year 1997 (revised as of December 10, 1997).

Discrimination appears particularly blatant in the automation rate categories. Presumably postal management grossly miscalculated that prior huge ratepayer investment in automated sorting equipment would produce cost savings. Now, they want nonprofits, who produce almost one-half their mail to meet the stringent requirements to qualify for automation rates versus 37 percent of their commercial counterpart's mail, to bear the brunt of postal management's miscalculation.

The exception is the automation rate category within the ECR Subclass for letters. Postal management would have both non-profit and commercial mailers bear equally in the expense to process mail with the automated sorting equipment. Assuming that this rate increase really reflects legitimate cost increases, it means that automated processing costs Standard A mailers three to four times more than the rate of increase of inflation.

(3) Corroborating evidence of discriminatory pricing

With one or two exceptions, the asymmetrical pricing treatment between comparable pieces of nonprofit and commercial Standard A mail suggests in and of itself discriminatory pricing. Two facts tend to confirm the prima facie evidence of bias.

First, the Postal Service has steadfastly refused to provide a straight forward explanation for its apparently biased pricing proposals in this rate case. Despite numerous opportunities to

respond to nonprofit intervenors' discovery attempts to explain what accounts for these proposed anomalous asymmetrical rates of change, postal management has ducked, dodged, and obfuscated.

Second, Ph.D. economists with many years of professional experience at both the Postal Service and Postal Rate Commission have been unable to unearth the full explanation. Admittedly, there is a limit to what these experts could uncover because the cost to access the Postal Service's data base and establish the accuracy of postal management's computations is prohibitive to nonprofit mailers.

Perhaps if nonprofit mailers could divert hundreds of thousands of dollars of charitable contributions to pay for computer time and specialists, they could discover how postal management has manipulated its cost data to produce these disparate rates of change.

It is also possible, however, that postal management has so skillfully covered its tracks that nonprofits might not be able to discover the answer even if they were able to raise hundreds of thousands of dollars from the public to pay for extensive computer analysis.

If the rationale for such disparate rates of change for comparable pieces of nonprofit and commercial mail were legitimate cost differences, one would think that postal management would lay these cards openly on the table. What would there be to hide, except perhaps mismanagement or misestimation? If there were mismanagement or miscalculation, however, it is grossly

unfair to propose that nonprofits alone bear those costs. Because postal management has not been forthright and experts are unable to derive a complete explanation for such disparate treatment of nonprofit and commercial Standard A mail, it reinforces the prima facie evidence of price discrimination.

C. This postal rate proceeding may not prevent discriminatory pricing.

It seems that a postal rate case has deteriorated into an expensive game, at least with respect to nonprofit rates, whereby postal management may successfully bury its cost data. Nonprofits lack the resources to replicate postal management's manipulation of its cost data.

The Postal Rate Commission faces limits too. For example, there are limits on the extent to which the Commission may compel the Postal Service to divulge forthrightly and coherently how it arrived at such disparate rates of change for nonprofit and commercial mail in the same rate categories, notwithstanding their similar handling characteristics.

The rules of the game seem to have come to this: Absent nonprofits having the wherewithal to unravel postal management's data compilations and computations, the Postal Service wins regardless of whether its proposed rates of change are "fair and equitable," regardless of whether they "bear the direct and indirect costs attributable" to nonprofit mail within each rate category of the Standard A class of mail, or regardless of

whether they represent "identifiable relationships between the rates or fees charged" comparable pieces of nonprofit and commercial Standard A as required by Sec. 3622(b)(1), (3), and (7) of the Postal Reorganization Act.

Congressional intent is thwarted if nonprofit mailers are unable to learn the postal monopolist's explanation for what appears on its face to be a discriminatory pricing scheme.

The anomalous asymmetrical differentials that postal management proposes for comparable pieces of nonprofit and commercial mail appear to circumvent the policy objective that Congress intended in the Revenue Forgone Reform Act, namely that changes in nonprofit rates would track changes in the comparable commercial rate. Moreover, rate regulation that cannot compel the Postal Service to lay its cards openly on the table or that does not provide rate relief when the monopolist leaves cards up its sleeve is regulation in form only.

Notwithstanding postal management's behavior toward nonprofit Standard A mail as manifested in its proposed rate scheme before the Commission, this proceeding may yet produce fair and equitable rates if the Commission were to be guided by the policy that Congress embedded in the Revenue Forgone Reform Act.

D. Conclusion

Postal management has not made its case that legitimate cost differences justify otherwise discriminatory pricing. Absent full disclosure and an opportunity to rebut, the Commission at a

minimum should recommend approximate symmetry in the rate of increase or decrease between nonprofit and commercial rates in the same rate category.

This is most important in the automation rate categories, where nonprofits produce almost one-half of their Standard A mail to possess exactly those qualities that postal management has repeatedly assured the Commission optimize mail handling.

II. Analysis of Proposed Disparate Rates of Change

Within the two Standard A rate subclasses for letter size mail pieces are nine rate categories. In two-thirds of those rate categories, the Postal Service proposes to adjust the rates of otherwise comparable nonprofit and commercial pieces in opposite directions. That is, within one rate category, postal management proposes to raise the rate for a piece of nonprofit mail while the rate for a comparable piece of commercial mail be rolled back.

For example, consider the non-automation rate category for letters within the Regular Subclass. Whether the piece serves a nonprofit or a commercial purpose, neither piece may be processed using the Postal Service's automated sorting equipment.

As for work sharing, there are two groups within the non-automation rate category: pieces that are sorted by like three- and five-digits and those residual pieces without even sufficient density for the mailer to sort them by three- and five-digits. That level of presort is called "basic."

With respect to the non-automation rate category at the basic presort level, the Postal Service has to do the maximum amount of work to process those pieces of mail, whether the piece serves a commercial or nonprofit purpose.

Despite these fundamental similarities in the lengths that the Postal Service has to go to in order to process each piece, the postal management proposes an absolute rollback of four

percent for the commercial piece of mail and a whopping 20 percent increase for the nonprofit piece. That's a swing of 24 percentage points for two pieces that are require essentially similar handling. See Table I below.

For pieces in the second presort tier within the non-automation rate category, the postal management proposes to leave the rate where it has been for mail that serves a commercial purpose but raise the rate by 19 percent for nonprofit mail. In effect, the postal management claims that it costs no more than before to process a piece of commercial mail that fails the characteristics needed in order to process it using the automated sorting equipment but is presorted to like three digits, but it now costs 19 percent more to handle the same piece of mail that serves a nonprofit purpose.

This same phenomenon--the rate for nonprofit and commercial mail moving in opposite directions within the same rate category --can be observed in two-thirds of nine rate categories that make up the two Standard A mail subclasses. See Table I below.

In two of the remaining three rate categories for letter size mail, the Postal Service proposes to increase the rate for both nonprofit and commercial mail pieces; however, the differential in one of the proposed rates of change is so large, one could call it asymmetric as well. In only one rate category does postal management propose to do what seems intuitively logical, and that is to increase each piece by the same factor.

Table I
Proposed Change in Standard A Mail Rates
for Commercial and Nonprofit Letters

Asymmetric Rates of Change

Subclass	Rate Category	Com- mercial	Non- profit	Differential in Percentage Points
-----	-----	-----	-----	-----
Regular	non-automation, basic presort	-4%	20%	24
Regular	non-automation, 3-/5-digit presort	0%	19%	19
Enhanced Carrier Route ("ECR")	saturation	1%	-17%	18
ECR	high density	1%	-16%	17
Regular	automation, basic presort	3%	18%	15
ECR	basic presort	9%	-3%	12
Regular	automation, 3- digit presort	0%	11%	11

Not only does postal management propose asymmetric rates of change for seven of the nine rate categories of Standard A letter-size mail, but also note the magnitude of the differential between the proposed rates of change for commercial and nonprofit Standard A mail. The smallest differential is 11 percentage points, and the largest is 24.

The magnitude of the differential for Standard A non-letter size mail is even greater. There are 17 rate categories for this type of Standard A mail. Two rate categories are omitted from

this analysis because the relatively low base on which the percentage has to be computed distorts the size of the percentage increase. A third is omitted because it didn't exist prior to this rate filing.

With respect to the remaining 14 rate categories, postal management proposes rates of change for eight rate categories that move in opposite directions depending on whether the non-letter size piece serves a nonprofit or commercial purpose. For the remaining six categories, in five of them postal management proposes to increase the rate for both nonprofit and commercial mail; however, the proposed rates of increase vary substantially.

In the sixth rate category for Standard A non-letter size mail, postal management proposes that a piece of nonprofit and commercial mail move in the same direction, and the differential is narrow, in this case it's two percentage points.

Table II below shows the magnitude of the differential in the Postal Service's proposed rates of change for the 20 of the 26 rate categories that make up Standard A mail. To recount, three rate categories are omitted because the rate of change is distorted for mathematical reasons. In a fourth rate category, postal management proposes to increase both nonprofit and commercial mail by the same amount. In the fifth and sixth rate categories, postal management proposes a differential that would be expected.

Table II

Magnitude of the Differential
Between Nonprofit and Commercial Standard A Mail
as Proposed by the U.S. Postal Service

	Average Differential Per Rate Category -----
Letters, Regular and ECR Subclasses (7 rate categories)	17 percentage points
Non-letters, Regular and ECR Subclasses (13 rate categories)	20 percentage points

Given the enormous differential in the proposed rates of change for mail that basically has similar characteristics relative to postal processing, one would expect that postal management could explain fully the economic reason for such disparate treatment.

That they have chosen not to and have resisted nonprofits' efforts to obtain full disclosure through discovery leads to the conclusion that discriminatory pricing is at work. This conclusion is buttressed further by the inability of recognized independent experts to penetrate postal management's data compilations and computations to determine how such disparate rates of change were generated for comparable pieces of nonprofit and commercial Standard A mail.

Respectfully submitted

National Federation of Nonprofits
By its attorneys:


George E. Miller
Nonprofit Service Group

December 30, 1997

CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document upon all participants of record in this proceeding in accordance with section 12 of the Rules of Practice.

A handwritten signature in cursive script, reading "George E. Miller", with a horizontal line drawn underneath it.

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December 30, 1997